Arizona Physicians IPA, Inc.

(Contract H0321)

Financial Statements as of and for the Years Ended December 31, 2007 and 2006, Supplemental Schedules as of and for the Year Ended December 31, 2007, and Independent Auditors' Report

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Arizona Physicians IPA, Inc.:

We have audited the accompanying balance sheets of Arizona Physicians IPA, Inc. (the "Company") as of December 31, 2007 and 2006, and the related statements of operations, changes in shareholder's equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States) and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental 2007 combining information on pages 16 and 17 and the quarterly reporting prepared using Arizona Health Care Cost Containment System ("AHCCCS") reporting guidelines for AHCCCS on the following pages are presented for purposes of additional analysis of the financial statements, rather than to present the financial position and results of operations of the individual lines of business, and are not a required part of the 2007 basic financial statements. These supplemental schedules are the responsibility of the Company's management. This information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Deloitte & Touche LLP

April 21, 2008

ARIZONA PHYSICIANS IPA, INC.

BALANCE SHEETS
AS OF DECEMBER 31, 2007 AND 2006
(In thousands)

	2007	2006
ASSETS		
CASH AND INVESTED ASSETS:		
Cash and cash equivalents	$ 6,676	$ 123,668
Investments (Note 4)	215,568	134,438
Total cash and invested assets	222,244	258,106
RECEIVABLES:		
Receivables from contract programs, net of allowances of $24, and $25, respectively (Note 9)	73,590	35,047
Investment income receivable	2,381	1,444
Other receivables	96	578
Total receivables	76,067	37,069
DEFERRED INCOME TAXES — Net	0	2,113
TOTAL	$ 298,311	$ 297,288
LIABILITIES AND SHAREHOLDER'S EQUITY		
LIABILITIES:		
Medical services payable (Note 8)	$ 189,905	$ 212,865
Due to affiliate — net	23,629	11,759
Payables to contract programs (Note 9)	5,436	18,362
Accounts payable and accrued expenses	2,701	950
DEFERRED INCOME TAXES — Net	129	0
Total liabilities	221,800	243,936
CONTINGENCIES (Notes 12 and 13)		
SHAREHOLDER'S EQUITY:		
Common stock, no par value — authorized, 1,000,000 shares; issued and outstanding, two shares	52,266	52,266
Retained earnings	22,438	353
Accumulated other comprehensive income	1,807	733
Total shareholder's equity	76,511	53,352
TOTAL	$ 298,311	$ 297,288

See notes to financial statements.

ARIZONA PHYSICIANS IPA, INC.

STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(In thousands)

	2007	2006
REVENUES:		
Capitation and risk-sharing settlements	$1,064,196	$1,014,744
Delivery supplemental premiums	61,499	61,069
Title XIX Waiver Group supplemental premiums	12,264	17,090
Investment income — net	12,420	11,529
Total revenues	1,150,379	1,104,432
MEDICAL SERVICES EXPENSES:		
Hospital inpatient services	346,965	352,175
Medical compensation	264,142	261,614
Other medical services (Note 11)	453,531	429,472
Reinsurance — net of premium	(72,565)	(60,230)
Total medical services expenses	992,073	983,031
ADMINISTRATIVE EXPENSES	103,183	102,646
PREMIUM TAXES	20,455	19,367
Total expenses	1,115,711	1,105,044
INCOME (LOSS) BEFORE INCOME TAXES	34,668	(612)
INCOME TAX EXPENSE (BENEFIT)	12,583	(1,023)
NET INCOME	$ 22,085	$ 411

See notes to financial statements.

ARIZONA PHYSICIANS IPA, INC.

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(In thousands)

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 22,085	$ 411
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Amortization of investment premium — net	953	398
Deferred income taxes	1,538	2,941
Gains on sale of investments — net	(343)	271
Change in operating assets and liabilities:		
Receivables from contract programs	(38,544)	(10,664)
Investment income receivable	(937)	(69)
Other receivables	482	(358)
Medical services payable	(22,959)	54,487
Accounts payable and accrued expenses	1,751	288
Payables to contract programs	(12,926)	(2,260)
Due to affiliate — net	11,870	4,423
Net cash (used in) provided by operating activities	(37,030)	49,868
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments available-for-sale	(102,028)	(79,607)
Maturities/sales of investments available-for-sale	22,066	27,756
Net cash used in investing activities	(79,962)	(51,851)
CASH FLOWS FROM FINANCING ACTIVITIES — Capital contribution	0	10,000
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(116,992)	8,017
CASH AND CASH EQUIVALENTS — Beginning of year	123,668	115,651
CASH AND CASH EQUIVALENTS — End of year	$ 6,676	$ 123,668

See notes to financial statements.

1. DESCRIPTION OF BUSINESS

Organization — Arizona Physicians IPA, Inc. (the "Company" or "APIPA") is a wholly owned, for-profit subsidiary of United HealthCare of Arizona, Inc. ("UHC of AZ"). UHC of AZ is a wholly owned subsidiary of United HealthCare, Inc., which in turn is a wholly owned subsidiary of United HealthCare Services, Inc. ("UHS"), a Minnesota corporation. UHS provides management services to managed care companies and is a wholly owned subsidiary of UnitedHealth Group Incorporated ("UHG").

The Company arranges medical care for its members through a contract with the Arizona Health Care Cost Containment System ("AHCCCS"), the state of Arizona's Medicaid program. The Company's other operations are through contracts with the Arizona Department of Economic Security Division for Developmental Disabilities ("DES/DDD") and with the Centers for Medicare and Medicaid Services ("CMS") for its Medicare Advantage health plan.

Beginning January 1, 2006, the Company began serving as a plan sponsor offering the Medicare Part D prescription drug insurance coverage under a contract with the Center for Medicare and Medicaid Services ("CMS"). The CMS premium and the member premium are recorded as capitation and risk-sharing settlements in the statement of operations. The Company is fully reimbursed by CMS for costs incurred for the catastrophic reinsurance and low-income premium subsidies, and, accordingly, there is no insurance risk to the Company. Amounts received for these subsidies are not reflected as premium revenues, but rather are accounted for as deposits, with the related liability recorded in medical services expenses in the statement of operations. The CMS risk share is a settlement with CMS that is based on whether the ultimate per member per month benefit costs of any Medicare Part D regional plan varies more than 2.5 percentage points above or below the level estimated in the original bid submitted by the Company and approved by CMS. The estimated risk share adjustment is recorded as an adjustment to premium revenues in the statement of operations.

The Company is undergoing a review with AHCCCS for a renewal of the contract effective October 1, 2008. The Company has a reasonable expectation that this contract will be renewed. The majority of the Company's revenue is derived from AHCCCS.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation — These financial statements have been prepared according to accounting principles generally accepted in the United States of America.

Use of Estimates — These financial statements include certain amounts that are based on the Company's best estimates and judgments. These estimates require the Company to apply complex assumptions and judgments, often because the Company must make estimates about the effects of matters that are inherently uncertain and will change in subsequent periods. The most significant estimates relate to capitation, risk sharing settlements, receivables from contract programs, medical services expenses and medical services payable. The Company adjusts these estimates each period, as more current information becomes available. The impact of any changes in estimates is included in the determination of income in the period in which the estimate is adjusted.

Revenue Recognition — Capitation revenues are recognized in the period in which enrollees are entitled to receive health care services. The Company records an HIV/AIDS supplemental premium for members who receive approved HIV/AIDS drugs in the month in which enrollees receive the approved drugs, which is included in capitation and risk-sharing settlements in the accompanying statements of operations. Delivery supplemental premium payments are per delivery and intended by AHCCCS to cover the cost of maternity care. Such premiums are recognized in the month that the delivery occurs. Title XIX Waiver Group ("TWG") supplemental premium payments are made for TWG members who are hospitalized on the date of application. Such premiums are recognized in the month of enrollment.

Cash and Cash Equivalents — Cash and cash equivalents primarily represent the Company's share of an investment pool sponsored and administered by UHS for the benefit of the UHS-owned health plans. The investment pool consists principally of investments with original maturities of less than one year, with the average life of the individual investments being less than 60 days. The Company's share of the pool represents an undivided ownership interest in the pool and is immediately convertible to cash at no cost or penalty. The pool is primarily invested in governmental obligations, commercial paper, certificates of deposit, and short-term agency notes, all of which are recorded at fair value. Interest income from the pool accrues daily to participating members based upon ownership percentage.

Investments — Investments consist of corporate bonds, government obligations, municipal securities, and commercial paper.

The Company follows the provisions of Statement of Financial Accounting Standards ("SFAS") No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and has classified all investments as available-for-sale, whereby investments are reported at fair value, with unrealized gains and losses reported as accumulated other comprehensive income, net of income taxes, in the statement of changes in shareholder's equity. Fair value is based on quoted market prices.

The Company continually monitors the difference between the cost and estimated fair value of its investments. If any of the Company's investments experience a decline in value that the Company believes is other than temporary, the Company records a realized loss in investment income in the statements of operations. No such impairment losses were incurred and recorded during the years ended December 31, 2007 and 2006.

Medical Risk Sharing — The Company has yearly risk-sharing agreements with AHCCCS to cover medical expenses in excess of certain limits established by the contract for TWG, Prior Period Coverage ("PPC") members and Social Security Disability Insurance – Temporary Medical Coverage ("SSDI") members. Receivables or payables and the corresponding revenues or contra-revenues are recorded depending on the surplus or deficit of revenues over medical and administrative expenses for the period.

Medical Services Expenses and Payables — Medical services expenses include claims paid, claims processed but not yet paid, estimates for claims received but not yet processed, and estimates for the costs of health care services enrollees have received, but for which claims have not yet been submitted.

The estimates for incurred but not yet reported claims are developed using actuarial methods based upon historical submissions and payment data, cost trends, customer and product mix, seasonality, utilization of health care services, contracted service rates, and other relevant factors. The estimates may change as actuarial methods change or as underlying facts upon which estimates are based change. The Company did not change actuarial methods during the years ended December 31, 2007 and 2006. Management believes the amount of medical services payable is adequate to cover the Company's liability for unpaid claims as of December 31, 2007 and 2006; however, actual claim payments may differ from those established estimates. Adjustments to medical services payable estimates are reflected in operating results in the period in which the change in estimate is identified.

Recently Issued Accounting Standards — In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 provides enhanced guidance for using fair value to measure assets and liabilities. It does not require any new fair value measurements, but does require expanded disclosures to provide information about the extent to which fair value is used to measure assets and liabilities, the methods and assumptions used to measure fair value, and the effect of fair value measures on earnings. In February 2008, the FASB issued FASB Staff Position SFAS 157-2, "Effective Date of FASB Statement No. 157" ("the FSP"). The FSP delayed, for one year, the effective date of SFAS 157 for all nonfinancial assets and liabilities, except those that are recognized or disclosed in the financial statements on at least an annual basis. Consequently, SFAS 157 will be effective for fiscal year 2008 for financial assets and liabilities recognized or disclosed in the financial statements. The deferred provisions of SFAS 157 will be effective for fiscal year 2009. The Company is currently evaluating the impact, if any, of the entirety of SFAS 157 on the financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115*. SFAS No. 159 permits companies to choose to measure financial instruments and certain other items at fair value at specified election dates. Unrealized gains and losses on items for which the fair value option has been elected shall be reported in earnings at each subsequent reporting date. SFAS No. 159 is effective for fiscal year 2008. This guidance will not have a material impact to the Company's financial statements.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140*. SFAS No. 155 (i) permits fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, (ii) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133, (iii) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, (iv) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives, and (v) amends SFAS No. 140 to eliminate the exemption from applying the requirements of SFAS No. 133 on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued during fiscal year 2007. The Company's adoption of this guidance did not have a material impact to its financial statements.

3. OPERATING AGREEMENTS AND RELATED-PARTY MATTERS

Pursuant to the terms of a management agreement, UHS will provide management services to the Company until terminated upon the written agreement of both parties, for a fee based primarily on a percentage of capitation revenue. Fees related to these arrangements totaled approximately $101,035,000 in 2007 and $97,928,000 in 2006 and are included in administrative expenses in the statements of operations. In addition, UHS pays, on the Company's behalf, certain general and administrative expenses not covered within the scope of the management agreement. UHS is reimbursed for these expenses by the Company and these expenses are included in administrative expenses in the statements of operations. Operations of the Company may not be indicative of those that would have occurred if it had operated as an independent company. The Company recorded approximately a reduction of $267,000 and an increase of $3,778,000 in 2007 and 2006, respectively, in loss adjustment expenses that are estimates of the amounts due UHS in the event that the Company's operations are discontinued. The Company has recorded a loss adjustment accrual of $3,510,811 and $3,778,000 as of December 31, 2007 and 2006, respectively.

The Company has an agreement with UHS to provide administrative services related to pharmacy management and claims processing for its enrollees. Fees related to these agreements totaled approximately $1,250,000 in 2007 and $1,218,000 in 2006 and are included in administrative expenses in 2007 and medical service expenses in 2006 in the statement of operations. Additionally, UHS collects rebates on certain pharmaceutical products and remits the rebates to the Company based on the Company's member utilization. Rebates received by the Company related to these agreements of approximately $6,955,000 in 2007 and $6,537,000 in 2006 are included as a reduction of medical services expenses in the statements of operations. Rebate receivables of approximately $185,000 in 2007 and $571,000 in 2006 are included as an offset to medical services payable on the accompanying balance sheets.

Beginning October 28, 2002, the Company entered into a $12 million subordinated revolving line of credit agreement with UHG at an interest rate of 30-day LIBOR plus a margin of 0.50%. The credit agreement is for a one-year term and automatically renews annually, unless either party gives written notice to the other party at least 60 days prior to the termination date of its intent to terminate the agreement. The agreement was automatically renewed effective October 28, 2006. No amounts were outstanding under the line of credit as of December 31, 2007 and 2006. Interest paid on amounts borrowed during the year under the line of credit totaled $13,000 in 2007 and zero in 2006.

4. INVESTMENTS

For purposes of calculating realized gains and losses on sales of investments, the amortized cost of each investment sold is used. The gross realized gains and losses on sales of investments totaled approximately $365,000 and zero, respectively, for the year ended December 31, 2007, and approximately $19,200 and $289,800, respectively, for the year ended December 31, 2006. The net realized gain or loss is included in investment income in the statements of operations.

As of December 31, 2007 and 2006, the amortized cost, fair value, gross unrealized holding gains and losses, and contractual maturities of the Company's investments, excluding cash and cash equivalents of $6,676,000 and $123,668,000, respectively, were as follows (in thousands):

	2007			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
U.S. government and agency	$ 47,441	$ 805	$	$ 48,246
State and state agency	65,777	1,015	(92)	66,700
Municipalities and local agency	52,137	580	(60)	52,657
Corporate bonds	47,224	770	(29)	47,965
Total	$ 212,579	$ 3,170	$ (181)	$ 215,568

	2007			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
Less than one year	$ 15,134	$ 78	$	$ 15,212
One to five years	73,466	1,541	(72)	74,935
Five to ten years	61,531	843	(39)	62,335
Over ten years	62,448	708	(70)	63,086
	$ 212,579	$ 3,170	$ (181)	$ 215,568

	2006			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
U.S. government and agency	$ 26,977	$ 34	$ (67)	$ 26,944
State and state agency	49,167	653	(125)	49,695
Municipalities and local agency	37,035	357	(90)	37,302
Corporate bonds	20,051	465	(19)	20,497
Total	$ 133,230	$ 1,509	$ (301)	$ 134,438

	2006			
	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
Less than one year	$ 4,062	$ 3	$ (3)	$ 4,062
One to five years	42,881	643	(44)	43,480
Five to ten years	63,634	613	(192)	64,055
Over ten years	22,653	250	(62)	22,841
	$ 133,230	$ 1,509	$ (301)	$ 134,438

Included in the U.S. government and agency securities in the tables above are mortgage-backed securities, which do not have a single maturity date. For the 2007 years to maturity table above, these securities have been presented in the maturity group based on the securities' final maturity date and at an amortized cost of $36,365,000 and a fair value of $36,870,000. For the 2006 years to maturity table above, these securities have been presented in the maturity group based on the securities' final maturity date and at an amortized cost of $17,059,000 and a fair value of $17,135,000.

As of December 31, 2007 and 2006, the Company had no investments in a continuous unrealized loss position for 12 months or greater. The unrealized losses are not material to the financial statements.

5. REINSURANCE AGREEMENT

Reinsurance reimbursements are recorded at estimated amounts due the Company pursuant to the AHCCCS and DES/DDD contracts. AHCCCS is required to reimburse the Company 75% (85% for catastrophic reinsurance) of qualified health care costs in excess of a reinsurance deductible of $15,000 or $50,000 (zero for catastrophic) per member per contract year through the contract ended September 30, 2007. Beginning October 1, 2007, AHCCCS is required to reimburse the Company 75% (85% for catastrophic reinsurance) of qualified health care costs in excess of a reinsurance deductible of $15,000 or $20,000 (zero for catastrophic) per member per contract year. For dates of service through September 30, 2005, DES/DDD was required to reimburse the Company 75% (85% for catastrophic reinsurance) of qualified health care costs in excess of the reinsurance deductible of $20,000 ($0 for catastrophic reinsurance) per member per contract year. Effective October 1, 2005, DES/DDD raised the reinsurance deductible to $100,000. Reinsurance recoveries of $43,775,000 and $28,738,000 have been included in receivables from contract programs net of allowances in the accompanying balance sheets as of December 31, 2007 and 2006, respectively. Reinsurance recoveries of approximately $72,565,000 for 2007 and $59,945,000 for 2006 have been offset against medical services expenses in the statements of operations.

APIPA had an agreement with ACE American Insurance Company to provide reinsurance coverage for members of its Medicare Advantage health plan. The agreement was effective from September 1, 2005 through August 31, 2006. Effective September 1, 2006, APIPA elected to self-insure for this line of business. Services eligible for recovery include inpatient and outpatient hospital services, skilled nursing facility services, and some intravenous and injectable pharmaceutical services. After the deductible of $100,000 is met, the co-insurance is 90% of eligible incurred claims. The reinsurance coverage has a $1,000,000 limit per person per agreement term. Reinsurance premium expenses of $759,000 for 2006 have been added to medical services expenses in the statements of operations. Reinsurance recoveries of zero and $95,000 have been included in receivables from contract programs in the accompanying balances sheets as of December 31, 2007 and 2006, respectively. Reinsurance recoveries of an unfavorable $4,000 for 2007 and a favorable $259,000 for 2006 have been offset against medical services expenses in the statements of operations.

6. PREMIUM TAXES

Effective October 1, 2003, the Company became subject to a 2% tax on all payments received from AHCCCS for premiums, reinsurance, and reconciliations.

7. INCOME TAXES

The Company's operations are included in the consolidated federal income tax return of UHG. Federal income taxes are paid to or refunded by UHG pursuant to the terms of a tax-sharing agreement under which taxes approximate the amount that would have been computed on a separate company basis. Federal income taxes payables of approximately $8,127,000 and receivables of approximately $5,298,000 at December 31, 2007 and 2006, respectively, are included in due to affiliate in the balance sheets. State income taxes payables of approximately $989,000 and $121,000 at December 31, 2007 and 2006, respectively, are included in accounts payable and accrued expenses in the balance sheets. Federal and state income tax refunds, net of payments was $3,247,000 during the year ended December 31, 2007. Federal and state income taxes paid, net of refunds was $4,203,000 during the year ended December 31, 2006.

The Company follows the provisions of SFAS No. 109, *Accounting for Income Taxes*, under which deferred income tax assets and liabilities are recognized for the differences between financial and income tax reporting bases of assets and liabilities based on enacted tax rates and laws. Total deferred income tax assets of approximately $1,053,000 in 2007 and approximately $2,592,000 in 2006 and total deferred income tax liability $1,182,000 in 2007 and approximately $478,000 in 2006 are included in the balance sheets. Deferred income taxes relate principally to required tax adjustments for medical services payable and unrealized gains.

The effective income tax rate reflects the Company's tax provision at the federal statutory rate, adjusted primarily for tax-exempt interest and state income taxes. The expense for income taxes for the year ended December 31, 2007 consists of a current federal income tax provision of $10,056,000, a current state income tax provision of $989,000, deferred federal income tax provision of approximately $250,000, and a deferred state income tax provision of approximately $1,288,000. The benefit for income taxes for the year ended December 31, 2006, consists of a current federal income tax benefit of approximately $4,084,000, a current state income tax benefit of approximately $447,000, a deferred federal income tax provision of approximately $3,020,000, and a deferred state income tax provision of approximately $488,000. Deferred income taxes relate principally to required tax adjustments for medical services payable and unrealized gains. In accordance with SFAS No. 109 and SFAS No. 115, the deferred income tax liability of approximately $1,182,000 and $478,000 at December 31, 2007 and 2006, respectively, resulting from the unrealized gain on investments, have been excluded from the deferred income tax provision and from the statements of cash flows.

In June 2006, the FASB issued Interpretation No. ("FIN") 48, *Accounting for Uncertainty in Income Taxes,* an interpretation of SFAS No. 109. On January 1, 2007, the Company adopted the provisions of FIN 48, *Accounting for Uncertainty in Income Taxes*. The Company has assessed the impact of FIN 48 on its financial condition, results of operations, and statement of cash flows and has determined that the result was not material to the 2007 financial statements. If at a time in the future the Company were to record unrecognized tax benefits, interest expense, and penalties associated with these amounts would be recorded as income taxes within the Company's financial statements.

As described in Note 1, the Company's operations are included in the consolidated federal income tax return of UnitedHealth Group. Federal income taxes are paid to or refunded by UnitedHealth Group pursuant to the terms of a tax-sharing agreement, approved by the Board of Directors, under which taxes approximate the amount that would have been computed on a separate company basis. Income taxes incurred in the current and prior years will be available for recoupment by the Company only in the event of future net losses of consolidated UnitedHealth Group. The Company receives a benefit at the federal rate in the current year for net losses incurred in that year to the extent the losses can be utilized in the consolidated federal income tax return of UnitedHealth Group Incorporated. UnitedHealth Group Incorporated currently files income tax returns in the U.S. federal jurisdiction, various states, and foreign jurisdictions. The U.S. Internal Revenue Service (IRS) has completed exams on

UnitedHealth Group Incorporated's consolidated income tax returns for fiscal years 2006 and prior. UnitedHealth Group Incorporated's 2007 tax return is under advance review by the IRS under its Compliance Assurance Program (CAP). With the exception of a few states, UnitedHealth Group Incorporated is no longer subject to income tax examinations prior to 2002 in major state and foreign jurisdictions. We do not believe any adjustments that may result from these examinations will be significant.

8. MEDICAL SERVICES PAYABLES

Changes in estimates related to prior years' incurred claims are included in medical services expenses in the current year in the statements of operations. The following tables disclose paid claims, incurred claims, and the balance in the unpaid claim reserve for the years ended December 31, 2007 and 2006 (in thousands):

	2007		
	Current Year Incurred Claims	Prior Years Incurred Claims	Total
Beginning year claim reserve	$ -	$ (212,865)	$ (212,865)
Paid claims	933,905	152,737	1,086,642
End of year claim reserve	184,462	5,443	189,905
Incurred claims	$1,118,367	$ (54,685)	$1,063,682

The above incurred claims do not include $562,000 in pharmacy rebates due from affiliate as of December 31, 2007. The above incurred claims do include $1,518,000 for Part D reinsurance amounts that is not included as Medical Payable.

	2006		
	Current Year Incurred Claims	Prior Years Incurred Claims	Total
Beginning year claim reserve	$ -	$ (158,124)	$ (158,124)
Paid claims	839,622	149,814	989,436
End of year claim reserve	207,233	5,632	212,865
Incurred claims	$1,046,855	$ (2,678)	$1,044,177

The above incurred claims do not include $1,883,000 in pharmacy rebates expense as of December 31, 2006. The above incurred claims do include $1,218,000 for Part D reinsurance amounts that is not included as Medical Payable.

9. MEDICAL RISK SHARING WITH CONTRACT PROGRAMS

The Company had a risk-sharing receivable related to TWG of $3,605,000 included in receivables from contract programs in the accompanying balance sheet as of December 31, 2007. The Company had a risk-sharing payable related to TWG of $15,230,000 included in payables to contract programs in the accompanying balance sheet of December 31, 2006. The TWG agreement was effective October 1, 2001 through September 30, 2006. The TWG agreement was renewed for the period October 1, 2007 through September 30, 2008. The Company had risk-sharing receivables related to PPC of $11,621,000 and $1,434,000 included in receivables to contract programs in the accompanying balance sheets as of December 31, 2007 and 2006, respectively. The Company has a risk-sharing receivable related to SSDI of $1,727,000 included in receivables to contract programs in the accompanying balance sheet as of December 31, 2007. The Company has payables in risk-sharing of $1,439,000, low income subsidy cost sharing (LICS) of $2,388,000 and reinsurance of $1,518,000 related to Medicare Part D program included in payables to contract programs in the accompanying balance sheet as of December 31, 2007. The Company had a payable in risk sharing of $1,231,000, low income subsidy cost sharing (LICS) of $1,245,000 and reinsurance of $639,000 related to Medicare Part D program included in payables to contract programs in the accompanying balance sheets as of December 31, 2006.

10. RESTRICTED ASSETS

Pursuant to its contracts with the state of Arizona and CMS, the Company is required annually to provide performance bonds, in an acceptable form, to guarantee performance of the Company's obligations under certain contracts. To satisfy this requirement, the Company maintained surety bonds in 2007 and 2006 in the amounts of $81,800,000 and $75,770,000, respectively. The three bonds are unsecured.

11. OTHER MEDICAL SERVICES EXPENSES

Other medical services expenses for the years ended December 31, 2007 and 2006 (in thousands), consist of the following:

	2007	2006
Pharmacy	$ 116,138	$ 101,249
Nursing facility and home health care	40,757	36,745
Emergency	64,753	66,667
Outpatient facility	72,950	69,653
Dental	41,387	40,011
Laboratory, x-ray, and medical imaging	41,723	42,485
Transportation	34,043	32,590
Durable medical equipment	20,702	18,559
Prior period coverage — other	14,766	15,665
Physical therapy	3,970	3,033
Other	2,342	2,815
Total	$ 453,531	$ 429,472

12. LITIGATION

The Company is involved in legal actions that arise in the ordinary course of its business. Although the outcomes of any such legal actions cannot be predicted, in the opinion of management, the resolution of these actions will not have a material adverse effect upon the financial position or results of operations of the Company.

13. COMMITMENTS AND CONTINGENCIES

Future contract awards are contingent upon the continuation of the AHCCCS and DES/DDD programs by the state of Arizona and the continuation of the CMS Medicare Advantage program and the Company's ability and desire to retain its status as a contractor under the programs. For the year ended December 31, 2007, substantially all of the Company's premium revenues were from these programs.

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ARIZONA PHYSICIANS IPA, INC.

SUPPLEMENTAL COMBINING BALANCE SHEET
AS OF DECEMBER 31, 2007
(In thousands)

	AHCCCS	DES/DDD	Medicare	Other	Total
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 6,676	$ -	$ -	$ -	$ 6,676
Investments	215,568	-	-	-	215,568
Total cash and invested assets	222,244	-	-	-	222,244
RECEIVABLES:					
Receivables from contract programs	64,982	4,835	3,797	-	73,614
Receivable from contract programs - allowances			(24)	-	(24)
Investment income receivable	2,381	-		-	2,381
Other receivables	25	1	70	-	96
Total receivables	67,388	4,836	3,843	-	76,067
RECEIVABLE BETWEEN CONTRACTS	-	5,087	60,253	(65,340)	-
TOTAL	$289,632	$ 9,923	$64,096	$ (65,340)	$298,311
LIABILITIES AND SHAREHOLDER'S EQUITY					
LIABILITIES:					
Medical services payable	$162,729	$ 5,534	$21,642	$ -	$189,905
Due to affiliate — net	12,737	154	10,761	(23)	23,629
Payables to contract programs	(240)		5,676	-	5,436
Accounts payable and accrued expenses	1,631	(23)	1,092	1	2,701
Deferred Income taxes - net	381	5	(257)	-	129
Total liabilities	177,238	5,670	38,914	(22)	221,800
PAYABLE BETWEEN CONTRACTS	65,347	-	-	(65,347)	-
SHAREHOLDER'S EQUITY					
Common stock	44,411	7,105	750	-	52,266
Retained earnings	829	(2,852)	24,432	29	22,438
Accumulated other comprehensive income	1,807	-	-	-	1,807
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	$289,632	$ 9,923	$64,096	$ (65,340)	$298,311

ARIZONA PHYSICIANS IPA, INC.

SUPPLEMENTAL COMBINING STATEMENTS OF OPERATIONS AND CHANGES IN ACCUMULATED SHAREHOLDER'S EQUITY FOR THE YEAR ENDED DECEMBER 31, 2007 (In thousands)

	AHCCCS	DES/DDD	Medicare	Other	Total
REVENUES:					
Capitation and risk-sharing settlements	$ 877,197	$ 42,759	$ 144,190	$ 50	$ 1,064,196
Delivery supplemental premiums	61,499	-	-	-	61,499
Title XIX Waiver Group supplemental premiums	12,264	-	-	-	12,264
Investment income — net	12,420	-	-	-	12,420
Total revenues	963,380	42,759	144,190	50	1,150,379
MEDICAL SERVICE EXPENSES:					
Medical services expenses:					
Hospital inpatient services	301,163	10,963	34,839	-	346,965
Medical compensation	239,757	7,352	17,033	-	264,142
Other medical services	384,409	27,924	41,198	-	453,531
Reinsurance - net of premium reimbursements	(65,480)	(7,097)	12	-	(72,565)
Total medical services expenses	859,849	39,142	93,082	-	992,073
Administrative expenses	85,912	4,431	12,840	-	103,183
Premium taxes	20,455	-	-	-	20,455
Total expenses	966,216	43,573	105,922	-	1,115,711
(LOSS) INCOME BEFORE INCOME TAXES	(2,836)	(814)	38,268	50	34,668
INCOME TAX (BENEFIT) PROVISION	(1,992)	(572)	15,128	19	12,583
NET (LOSS) INCOME	(844)	(242)	23,140	31	22,085
SHAREHOLDER'S EQUITY — Beginning of year	33,817	4,495	15,042	(2)	53,352
EQUITY TRANSFER	13,000	-	(13,000)	-	-
OTHER COMPREHENSIVE GAINS	1,074	-	-	-	1,074
SHAREHOLDER'S EQUITY — End of year	$ 47,047	$ 4,253	$ 25,182	$ 29	$ 76,511